ARNOLD & PORTER LLP

David F. Freeman, Jr.
David.Freeman@aporter.com

202.942.5745
202.942.5999 Fax

555 Twelfth Street, NW
Washington, DC 20004-1206

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Elizabeth M. Murphy
Secretary
U.S. Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549-1090

Re: Family Offices, Proposed Rule
Release No. IA–3098; File No. S7–25–10

Dear Ms. Murphy:

We appreciate the opportunity to comment on the above-referenced rulemaking proposal (the "Release")[1] that will implement Section 409 of the Dodd-Frank Wall Street Reform and Consumer Protection Act (the "Dodd-Frank Act"). Section 409 of the Dodd-Frank Act amended the Investment Advisers Act ("Advisers Act"), 15 U.S.C. § 80b, by adding a new Section 202(a)(11)(G) which authorizes the Commission to adopt a rule exempting "family offices" from the Advisers Act. Since 1940, the SEC has had authority to grant exemptions from the Advisers Act to family offices by individual order, and has done so on many occasions over the past 70 years.[2] Proposed Rule 202(a)(11)(G)–1 (17 C.F.R. § 275.202(a)(11)(G)–1) will implement the new authority.

[1] SEC, *Family Offices* (Proposed Rule), 75 Fed. Reg. 63753 (Oct. 18, 2010).

[2] *WLD Enterprises, Inc.*, Rel. No.IA- 2807 (Nov. 14, 2008); *Woodcock Financial Management Company, LLC*, Rel. No. IA-2787 (Sept. 24, 2008); *In the Matter of Slick Enterprises Inc.*, Rel. No. IA-2745 (June 20, 2008); *In the Matter of Gates Capital Partners, LLC and Bear Creek, Inc.*, Rel. No. IA-2599 (Mar. 20, 2007); *In the Matter of Adler Management, L.L.C.*, Rel. No. IA-2508 (April 14, 2006); *In the Matter of Riverton Management, Inc.*, Rel. No. IA-2471 (Jan. 6, 2006); *In the Matter of Parkland Management Company, L.L.C.*, Rel. No. IA-2369 (March 22, 2005); *In the Matter of Longview Management Group LLC*, Rel. No. IA-2013 (Feb. 7, 2002); *In the Matter of Kamilche Company*, Rel. No. IA-1970 (Aug. 27, 2001); *In the Matter of Bear Creek Inc.*, Rel. No. IA-1935 (April 4, 2001); *In the Matter of Moreland Management Company*, Rel. No. IA-1705 (March 10, 1998); *In the Matter of The Pitcairn Company*, Rel. No. IA-52 (March 2, 1949); *In the Matter of Roosevelt & Son*, Release No. IA-54 (August 31, 1949); and *In the Matter of Donner Estates, Inc.*, Rel. No. IA-21 (November 3, 1941).

We take as a premise for this rulemaking that the intent of the Commission is to adopt a rule with provisions broad enough to include normal familial arrangements and relationships that are reflected in the practices of *bona fide* family offices, in order to avoid dislocations at family offices and a rush of exemptive applications and registrations at the Commission, while not drawing the provisions so broadly as to allow evasion of the Advisers Act and abuse of investors under the guise of the family office exemption by firms providing services to persons and entities outside of normal familial relationships.

Our comments relate to clarification of four points: (1) ownership of a family office through trusts for family members; (2) impact of future and residual interests in trusts on their status as "family clients" under the proposed rule; (3) sponsorship of pension and employee benefit plans by the family office, and (4) who is the "founder" from whom lineal descent is measured. We also suggest broadening the definition of "family clients" to include any trusts created and funded solely by family members in which non-transferrable interests are gifted to relatives of spouses of family members.

Meaning of "Direct or Indirect" Ownership In Subsection 202(a)(11)(G)-1(b)(2)

One of the requirements under the proposed rule for a company to qualify as a family office is that the company is "wholly owned and controlled (directly or indirectly) by family members." It is our understanding that the term "indirectly" in the proposed text is intended to include ownership by family members indirectly through one or more trusts. We suggest, for the sale of clarity, that the text of this clause be revised to read "wholly owned and controlled (directly or indirectly) by ***or for the benefit of*** family members" (new text highlighted). It is common for a family office to be owned through one or more trusts for the benefit of family members. The Commission has previously approved this ownership structure for family offices through individual orders.[3] In the alternative, the adopting release could include a statement clarifying that ownership through one or more trusts for the benefit of family members is included within the meaning of "directly or indirectly."[4]

[3] *Longview Management Group LLC*, Release Nos. IA-2008 (Jan. 3, 2002) and IA-2013 (Feb. 7, 2002); *Moreland Management Company*, Release Nos. IA-1700 (Feb. 12, 1998) and IA-1706 (Mar. 10, 1998); *In the Matter of Donner Estates, Inc.*, Release No. IA-21 (Nov. 3, 1941).
[4] The same textual issue occurs in the Subsection (d)(2)(v) definition of "family client" as including companies "wholly owned and controlled (directly or indirectly) by, and operated for the sole benefit of, family members…." We similarly suggest that either the words "*or for the benefit of*" be added to the text of this subsection after "by" or the

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Future and Residual Interests in Family Trusts

Under the proposed rule, a family office can only provide advisory services to "family clients." A trust qualifies as a "family client" that can be served by an exempt family office, provided that the trust is "existing for the sole benefit of one or more family clients." Trusts are commonly created by individuals or married couples to benefit themselves and their lineal descendants. Trusts can last a very long time, and the distribution of income and benefits from the trust changes over time. Who is now and who will in the future be the beneficial owners of the trust generally is established under rules set out in the trust, and under applicable property and trust laws. Depending upon events that unfold over time, births and deaths, and changes in circumstances, these rules are applied to determine who gets what from the trust at that point in time. More often than not, trust instruments include provisions for the future distribution under some circumstances of income or assets to persons or entities that are not lineal descendants. This might be a favored friend or collateral relative, a college, a religious group, or some other public charitable organization or foundation. Most often, this is to avoid distribution to "laughing heirs" (distant relatives who would take under applicable state succession laws if there are no surviving beneficiaries named under the trust) or escheat to the state if the designated beneficiaries do not live long enough to receive their interest. Inclusion of such provisions in the trust instrument is, essentially, an estate planning tool much like a will.

We understand the plain meaning of the term "existing" used in the proposed rule to mean in the here and now, rather than at some future time. Accordingly, we understand the proposed rule to look to who currently is an income beneficiary of a trust or otherwise currently enjoys the use of the property of the trust (whether under a life estate, a term of years or some other measuring stick, and regardless of whether they have a right to invade principal or have powers of appointment) to determine whether a trust qualifies as a "family client" under the proposed rule. Future interests, whether contingent or not and whether vested or not, would not be considered. If this is not what is intended, it would be appropriate to so state in the adopting release. But in that case, we anticipate that there will not be very many trusts that qualify as "family clients" and

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adopting release state that beneficial ownership through trusts is within meaning of "indirectly."

the Commission will be inundated with family offices either seeking an individual exemptive order from coverage under the Advisers Act or seeking to become registered under the Advisers Act, which would defeat the purpose of Section 409 of the Dodd-Frank Act. Moreover, it is difficult to imagine how permitting a family office to service family trusts that contain what are nearly universal clauses which name persons or entities that are neither lineal descendants of the founder nor charities founded by the family, as future or potential future beneficiaries that, if they get anything at all will receive it as a gift, could lead to abuse or permit public advisers to evade the Advisers Act by masquerading as family offices.

Family Office Pension and Employee Benefit Plans

Family offices sponsor pension and employee benefit plans and provide services to them. These include qualified and non-qualified plans, and are normal compensation arrangements for employees. They are put in place at family offices, just as they are at other companies, to allow the family office to attract and retain qualified personnel. In Section 409(b)(2) of the Dodd-Frank Act, Congress directed the Commission in its rulemaking to "recognize[] the range of ... employment structures and arrangements of family offices." This direction would appear to include the employee benefit and compensation programs of a family office and its parent company and their predecessor entities. Accordingly, we suggest that the final rule, the adopting release, or a letter issued by the Staff at the time the final rule is adopted, make clear that family offices are not disqualified from reliance on the exemption provided by the rule by providing services (without compensation) to pension and employee benefit plans for which the family office or its parent company is the plan sponsor.

Employer-sponsors of pension and employee benefit plans perform a variety of tasks, including service as trustee or review and selection of trustees and plan fiduciaries, approval of investment options and reports of trustees and plan advisers, and other tasks that could literally be read to fall within the broad definition of "investment advice" under the Advisers Act. In a series of letters issued to the Department of Labor, the Commission Staff made clear that the normal employer/employee relationships represented by pension and employee benefit plans are not the sort of relationship at which the Advisers Act was directed.[5] The amendment by the Dodd-Frank Act of the Advisers Act to remove, effective July 21, 2011,

[5] *Employer-Sponsors of Defined Contribution Plans*, Letters to Olena Berg, U.S. Department of Labor, from Jack Murphy, Associate Director and Chief Counsel, Division of Investment Management (avail. Dec. 5, 1995 and Feb. 22, 1996); *accord, Lockheed Martin Investment Management Company*, SEC Staff Letter (avail. June 5, 2006).

the old "fewer than fifteen clients" exemption from the Advisers Act puts this issue front and center for all companies that have pension and employee benefit plans. It may be appropriate for the Commission to reiterate this Staff position in the adopting release or an accompanying Staff letter, so that the many thousands of employer-sponsors of pension and employee benefit plans will not wonder whether they become subject on July 21, 2011 to registration under the Advisers Act.

Definition of "Founders"

The term "founder" is used in the proposed rule to establish the person from whom lineal descent is traced to define the "family members" who can be owners and clients of the family office. Subsection (d)(5) defines "founders" as the natural person and spouse or equivalent for whose benefit the family office was established. In many cases, the founder who generated the family wealth has long since passed away. Family offices are often organized or reorganized after that founder is no longer alive.

In some cases, the family office evolved from its roots as an operating company or the holding company for one or more operating businesses, with the various business units divested over time and the proceeds remaining in the family office or an affiliate. In some cases even when the founding person was still alive at the time of formation of the family office, the family office was formed to manage the affairs of the descendants, rather than of the founder.

We suggest that the definition of "founders" make clear that (1) the exemption is not lost if the founders are no longer alive, (2) the exemption carries over to any reorganized or successor entities that provide the family office services, and (3) the "founder" can be the person who generated the family wealth or who built the business or company that generated the family wealth, even if the company that is the family office was formed later to manage that wealth for the descendants of that founder.

Trusts Established and Funded by Family Members for Spouse's Family Members

It is not uncommon for a person to establish and fund a trust for the benefit of a family member, to provide for the future support of that person. That type of gifting decision is commonly made jointly by married couples in respect of their family members. The recipient of the beneficial ownership of such a trust is happy to have it. They paid nothing for it, and they will eventually receive the benefit of it. Generally it is put in trust, rather than given as cash, so that the money will be there when needed. When spouses make these decisions, they are just as likely to bestow this largess upon the blood relatives of one spouse as the other. Because the money is a gift, it is hard to imagine how a family office could cater to the public or otherwise evade the Advisers Act by servicing this type of family trust.

The terms we use to define the family members of married couples reflect the reality of how family relationships operate, and they do not strictly follow lineal descent. My sister's husband is my brother-in-law. My wife's brother is also my brother-in-law. His wife is my sister-in-law. Their respective daughters are my nieces. There is not a separate term for "niece-in-law," or for "sister-in-law-in-law."

Yet by the way in which the list of family members is defined in the proposed rule, distinctions are drawn between the ability of a married couple, one of whom is a lineal descendant of the founder, to gift trust interests in a trust serviced by the family office to the lineal descendant's sibling's child (the "niece") as opposed to the spouse's sibling's child (the "niece-in-law"). As noted above, however, there is no such thing as a "niece-in-law." The unlucky lineal descendant who seeks to explain to his or her spouse, in connection with a gifting decision, the definition of the term "family member" in subsection (d)(3) of the proposed rule, would be well-advised first to consider subsection (d)(4) of the rule.

If the guiding principle in defining the outlines of what are permitted family clients of a family office in the context of the permitted beneficial owners of trusts established and funded entirely by family members, involves balancing whether permitting the practice opens up the opportunity to use the family office exemption to evade the Advisers Act against whether the practice is common to family offices and family trusts that they service and thus if not permitted within the exemption could result in family office dislocations, exemptive applications and registrations, the scales weigh in favor of a broader definition of permitted family member beneficiaries of gifted interests in trusts to include family members of spouses (and spousal equivalents) of lineal descendants.

We appreciate the opportunity to comment on the Release and thank you for your consideration of these comments. If you have any questions or wish to discuss them further, please do not hesitate to contact me at (202) 942-5745.

Sincerely,

David F. Freeman, Jr.